BLENDED CREDITS FOR COTTON TO KOREA

Issue:

On March 17, the SIG-IEP opposed (8-2) an Agriculture proposal to extend a 3-year $50 million blended credit to finance U.S. cotton exports to Korea. As a result of considerable congressional and industry displeasure with the SIG's decision, the Administration has agreed to review once again the merits of the transaction at the IG level. Arguments for and against the transaction can be summarized as follows:

Pros:

(1) Korea is the second largest foreign market for U.S. cotton, accounting for nearly 30 percent of total U.S. cotton exports. Korea is the seventh largest market for all U.S. agricultural commodities. We should not alienate this loyal customer whose market we have so carefully developed.

(2) The U.S. share of the Korean cotton market has been over 90 percent for the last ten years. Cheaper foreign competition, some of which is subsidized, is eroding this market share. The cotton industry reports that from December 1982 through January 1983, the U.S. share dropped to 80 perent. Blended credits may help turn this trend around.

(3) There is a large surplus of cotton in the United States which has kept prices depressed. $50 million of blended credits to Korea are estimated to provide additional exports of 86,000 bales. Reduction of domestic stocks by 86,000 would remove cotton which otherwise could go under loan at a cost of $24.5 million.

(4) The Korean textile industry has threatened to reduce its cotton imports from the United States if they do not receive blended credits, resulting in a far greater loss of exports than 86,000 bales, and even higher CCC net outlays for the cotton program. The industry estimates a possible decrease in market share over the next three years to 60 percent, if the Korean textile industry does not receive blended credits.

(5) Extension of blended credits to Korea will not increase Korean textile exports to the United States since they are limited by a bilateral agreement under the MFA.

Cons:

(1) With its high credit rating, Korea has access to private capital markets. For FY 83, CCC has already authorized $300 million in

export credit guarantees to Korea to finance U.S. cotton exports on 2-1/2 year terms. This represents over 40 percent of Korea's total annual cotton imports. Additional U.S. Government subsidized credit is not necessary.

(2) Korea pays cash for the majority of its imports from non-U.S. suppliers -- India, Sudan, Pakistan, Egypt. Blended credits have a strong potential to displace these non-subsidized suppliers. Since its devaluation, Brazil, a minimal cotton supplier to Korea, has eliminated its export price subsidy for cotton.

(3) Three-year blended credits for cotton are excessive. Normal turnaround time from cotton imports to textile exports is 6-12 months. By offering 3-year blended credits, the U.S. Government is providing a subsidized working capital loan to the Korean textile industry.

(4) Extension of blended credit would completely undermine (i) U.S. efforts to move Korea gradually to cash or at most 1-year CCC terms and (ii) the existing U.S. Government/Korean agreement to decrease cotton terms to 2-1/2 years in FY 83, 2 years in FY 84, etc.

(5) We may be buying our own cotton market, substituting blended credits for cash or CCC-guaranteed sales, rather than promoting "additional" cotton exports. Extension of blended credits would have little or no impact on CCC outlays unless any "additional" cotton exported comes from stocks on loan to CCC.

(6) Extension of this $50 million of subsidized credit would only be the beginning. The Korean textile industry will be back demanding more subsidized credits and an increase in term on the guaranteed credit back to three years, if the United States wants to retain its 90 percent market share.

Options:

1. Reaffirm the decision of the SIG.

2. Recommend that the SIG reconsider the proposal, and approve the $50 million blended credit for cotton to Korea.

3. Option Number Two with the caveat that Korea will receive no further blended credits.

April 27, 1983